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In the Supreme Court of the United States

OCTOBER TERM, 1962

No. 253

J. G. BOSWELL COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 47-66) are reported at 34 T. C. 539. The opinion of the Court of Appeals (Pet. App. 1-11) is reported at 302 F. 2d 682.

JURISDICTION

The judgment of the Court of Appeals was entered on April 17, 1962 (Pet. App. 12). The petition for a writ of certiorari was filed on July 14, 1962.

The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the courts below correctly held that the temporary interruption of the use of farmlands, which were rehabilitated by the taxpayer after they had been flooded, was not a loss of capital for which a deduction may be allowed under Section 23(f) of the Internal Revenue Code of 1939, but was, rather, a loss of potential income for which no deduction is allowable.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) *Losses by Individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

* * * * *

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. No loss shall be allowed as a deduction under this paragraph if at the time of the filing of the return such loss has been claimed as a deduction for estate tax purposes in the estate tax return.

(f) *Losses by Corporations.*— In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

(26 U.S.C. 1952 ed., Sec. 23.)

Treasury Regulations 111 (1939 Code):

Sec. 29.23(e)-1. *Losses by individuals.*

* * * * *

In general losses for which an amount may be deducted from gross income must be evidenced by closed and completed transactions, fixed by identifiable events, bona fide and actually sustained during the taxable period for which allowed. Substance and not mere form will govern in determining deductible losses. Full consideration must be given to any salvage value and to any insurance or other compensation received in determining the amount of losses actually sustained. * * *

* * * * *

Sec. 29.23(f)-1. *Losses by Corporations.*— * * * The provisions of sections 29.23(e)-1 to 29.23(e)-5, inclusive, * * * are in general applicable to corporations as well as individuals. * * *

Sections 39.23(e)-1 and 39.23(f)-1 of Treasury Regulations 118 (1939 Code), applicable to taxable years beginning after December 31, 1951, are substantially the same as the provisions of Regulations 111 set forth above.

STATEMENT

Petitioner, J. G. Boswell Company, a California corporation, is the successor by merger in 1957 of the Tulare Lake Land Company and the J. G. Boswell Company, both of which owned and operated farms in the Tulare Lake Basin in Kings County, California (Pet. App. 1-2). Petitioner claims loss deductions for its predecessor companies in fiscal years ending June 30, 1952, and March 31, 1953, by reason of the flooding of the lands in the spring of 1952.

The basin is a reclaimed lake bed and is the natural repository for snow melt run-off waters of several streams. It is not unusual for water to settle there because the lowest natural outlet is nearly thirty feet above the floor of the basin. Flooding waters in time sink into the soil, evaporate, or are removed by pumping. But the water often remains many weeks before it is entirely removed and the presence of the water prevents normal use of the land (Pet. App. 3).

Approximately four feet below the surface is a hard clay pan which for practical purposes is impervious to water. As a result, the soil directly above the pan has accumulated a high content of salt deposits from floods and irrigation waters. Salt tends to inhibit the growth of crops. However, successful farming is possible through a combination of leaching and other farming techniques such as deep plowing, mulching, and rotation of crops (Pet. App. 3).

The basin has a history of periodic flooding. Since 1940 it has been flooded in each of the years 1940,

1942, 1943, 1952, 1955 and 1958 (R. 50). The flooding waters of 1952 had a high salt content but there was no evidence of the salt content of the soil at the time of the flood or immediately after the lands had been de-watered (Pet. App. 3).

The flood reached its crest about June 30, 1952, and petitioner's land was covered with twelve to fifteen feet of water. The action of the water caused breaks in the levees, washed soil around, deposited silt in the drainage and irrigation ditches and left the land in an uneven and rough condition (Pet. App. 3-4).

Pumping off the flood waters from one of petitioner's parcels was completed as early as February 23, 1953, and by September 22, 1953, all the remaining parcels had been pumped dry. Petitioner also repaired the other damage to its lands and, as soon as the land was de-watered and repaired, the soil was prepared for farming, crops were planted and the normal operation of the farms was resumed. The cost of the rehabilitation of its lands was deducted by petitioner, and allowed by the Commissioner, as a business expense. Production on most of the land equaled or exceeded the pre-flood output (Pet. App. 4).

The Tax Court upheld the Commissioner's disallowance of the petitioner's estimated loss which in effect represented a loss of profits (R. 58). The Court of Appeals affirmed the Tax Court's decision (Pet. App. 1-11).

ARGUMENT

The decision below is correct and there is no reason for further review of this case.

1. Petitioner now seeks to justify its claim of a loss solely on the ground that "it would lose the use of its land for a period of time—that is, as long as the land remained under water." (Pet. 10). The sole question presented is whether this temporary loss of use, or loss of potential income, is a loss deductible under Section 23(f), *supra*, p. 3. That section requires an actual loss of capital occurring during the year for which the deduction is claimed which is evidenced by a closed and completed transaction, fixed by identifiable events. *Hort* v. *Commissioner*, 313 U. S. 28; *A. Giurlani & Bro.* v. *Commissioner*, 119 F. 2d 852 (C. A. 9th); Treasury Regulations 111, Sections 29.23(e)-1 and 29.23(f)-1, *supra*, p. 3. A merely temporary shrinkage or diminution in value of property is not sufficient to establish a loss of capital. *Denise Coal Co.* v. *Commissioner*, 271 F. 2d 930 (C. A. 3d); *Pugh* v. *Commissioner*, 49 F. 2d 76 (C. A. 5th), certiorari denied, 284 U. S. 642.

The flood temporarily interrupted petitioner's farming. Petitioner consequently was deprived of the functional benefit of its land for a short period. At no time, however, was petitioner's prospective use of the land for farming purposes permanently and irrevocably lost. Petitioner knew the ephemeral conse-

In the court below, petitioner asserted the three additional elements of physical injury to its lands, a permanent increase of salts to its soil and the unavailability to it of a "cotton history" for its land. (Pet. App. 2.) The court of appeals rejected petitioner's argument that these elements supported its claim of a deduction for a capital loss (Pet. App. 8-11), and petitioner has now abandoned those claims (Pet. 9-10).

quences of the flood to its business; it knew that modern farming techniques would recondition the land. Petitioner had previously purchased land while it was under water, reconditioned the land and began farming it within a short time (Pet. App. 7). In fact, more than one-half of the land on which the loss is claimed (approximately 10,800 acres of the 19,000 acres involved) was rehabilitated within eight months after the flood and the remaining acreage was rehabilitated within seven months thereafter (Pet. App. 4, R. 49, 51). Petitioner deducted the cost of rehabilitation as a business expense, and its farming business was resumed.

Since the use of the land for farming was never irretrievably lost, petitioner was only denied the realization of income which farming might have produced for the period of the interruption. The loss of potential income is not a deductible capital loss. As this Court said in *Hort* v. *Commissioner*, 313 U. S. 28, 32-33:

> Nothing in § 23(e) indicates that Congress intended to allow petitioner to reduce ordinary income actually received and reported by the amount of income he failed to realize. * * *

The facts do not show that petitioner otherwise parted with anything of value which is equivalent to a loss of capital. There was no irreparable physical

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The court referred to Section 23(e), the loss provision covering individuals. The same principles are applicable under Section 23(f) which is the loss provision covering corporations. See p. 3, *supra*.

damage to the income-producing property; nor was there a sale, abandonment or other disposition of the property to fix a capital loss. In short, the requisite closed and completed transaction with respect to the income-producing farmland itself is lacking. Even if the flood adversely affected the ultimate value of the farmland, that injury is not deductible until a closed and completed transaction fixes the extent of the loss. *Hort* v. *Commissioner*, 313 U. S. 28, 33; *United States* v. *White Dental Co.*, 274 U. S. 398, 401; *Citizens Bank of Weston* v. *Commissioner*, 252 F. 2d 425, 427 (C. A. 4th).

2. Contrary to petitioner's contentions (Pet. 11-13, 14-19), the decision below is not in conflict with decisions of this Court or of courts of appeals. In urging a conflict with *United States* v. *White Dental Mfg. Co.*, 274 U. S. 389, petitioner asserts that the loss of use in that case was not permanent (Pet. 11). But this Court decided that the use was completely lost upon the German Government's seizure of the corporate property and that whether anything would be returned was "dependent upon the hazards of the war then in progress" and, thus, highly remote. 274 U. S. at 402. Accordingly, the seizure was deemed a closed

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All the cases cited by petitioner as in conflict with the decision below are distinguishable. *Helvering* v. *Owens*, 305 U. S. 168, involved two casualties and the court determined the extent of the loss. There is no indication that any question of temporary impairment of use was raised or decided in that case. The cases dealing with a "taking" of property (Pet. 11-13) were properly described by the court below as involving a permanent impairment of usefulness (Pet. App. 6-7) and, hence, inapposite.

and completed transaction sufficient to establish the worthlessness of the investment and to establish the right to a loss deduction.[1] By contrast, petitioner here suffered a mere short-term deprivation which, from the outset, was known to be only temporary.

There is no conflict with *Hort* v. *Commissioner*, 313 U. S. 28 (Pet. 14-17). That case does not suggest that the taxpayer might have had a deductible loss because he collected less through the cancellation than he would have if the lease had run its full course. The Court merely adverted to a deduction covering diminution in the value of the property, if such a loss could be established by a closed transaction. 313 U. S. at 33. But the loss of rental income was itself expressly held non-deductible. *Id.*, at 32-33. Thus, here, the loss of potential income did not become a loss of capital because merely petitioner was able to show a basis for its farmlands.

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[1] Petitioner's argument with respect to proof of the diminished value of its farmlands (Pet. 17-19) misses the point because, as we have shown, nothing occurred here which fixed a loss based on shrinkage in value.

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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No. 253

J. G. BOSWELL COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

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Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

ARGUMENT.

1. The Decision Below Conflicts With Decisions of This Court That Casualties Constitute Transactions on Which Losses Can Be Deducted.

On page 6 of the Brief for the Respondent in Opposition the respondent cites as authorities for the proposition that in order to take a loss of capital there must be a closed and completed transaction fixed by an identifiable event: *Hort v. Commissioner*, 313 U. S. 28; *A. Giurlani & Bro. v. Commissioner*, 119 F. 2d 852 (C. A. 9th); Treasury Regulations 111, Sections 29.23 (e)-1 and 29.23(f)-1.

The petitioner, of course, concedes the proposition stated, but submits that neither of the cases cited throw

any light on the question of whether the flood constituted a closed and completed transaction. The Court below found that the flood constituted an identifiable event fixing the onset of the damage, if any. (Pet. App. 5.)

In neither case cited was there a casualty involved. Both cases dealt with transactions initiated by the taxpayers for their own over-all benefit. Then they claimed that the burdens associated with such transactions caused deductible losses.

In *Hort v. Commissioner, supra*, the taxpayer voluntarily cancelled a lease upon receipt of $140,000. It had no cost for the lease, and, hence, could not have a loss, as a loss is the difference between cost of an asset given up and the amount received therefor. Furthermore, the transaction amounted to a collection of a receivable, and not the sale of an asset, *Hale v. Helvering*, 85 F. 2d 819, 821 (A. D. C.); *Bingham v. Commissioner*, 105 F. 2d 971, 972 (C. A. 2). Consequently, there could be no closed transaction on which to base a loss.

In *A. Giurlani & Bro. v. Commissioner, supra*, the taxpayer paid the debt of a supplier of olive oil and claimed a loss to be deductible. The Court said at page 857:

> "That the payment or expenditure was deliberate and intentional, made by the taxpayer for the insuring of its profits for future years. In the sense that no enforceable obligation existed against it, the expenditure was voluntary."

Hence, these two cases throw no light whatsoever on the question of whether this flood, depriving petitioner

of the use of its farmlands for a period of time and hence reducing its value, was a closed and completed transaction, fixed by an identifiable event.

Also on page 6 of the respondent's brief, he states that a merely temporary shrinkage or diminution in value of property is not sufficient to establish a loss of capital. As authorities, he cites *Denise Coal Co. v. Commissioner*, 271 F. 2d 930 (C. A. 3d), and *Pugh v. Commissioner*, 49 F. 2d 76 (C. A. 5th), certiorari denied, 284 U. S. 642.

Neither of these cases turned on the question of whether the injury was temporary or permanent, and therefore they are not apposite on the point for which they were cited.

Both cases more nearly approach the question of whether there was a closed or completed transaction fixed by an identifiable event.

In *Denise Coal Company, supra*, the taxpayer had adjoining pieces of land. On one it carried on strip mining operations, and on the other, on which the loss was claimed, it contended that the value of the land for the agricultural purposes for which it was acquired, had been destroyed because the soil had been permeated by acids from waters on deposits thrown up in the coal mining operations.

The Court disallowed the loss for several reasons: First, the taxpayer did not claim that the land was worthless for all purposes, but only the surface for agricultural purposes; second, that injury to the land occurred yearly, so it was not possible to find an identifiable date on which injury occurred; and, third, the injury was self-induced and was not a casualty.

Likewide, in *Pugh v. Commissioner, supra*, the injury complained of was self-induced. There the taxpayer leased agricultural land for oil production. Oil was found and produced, but the operation of the oil lease impregnated the land with oil and salt and made the surface unfit for cultivation. Taxpayer claimed a loss for a reduction in the value of agricultural rights. The Circuit Court properly said at page 77:

> "The land has simply been turned from its former agricultural use to another use which it believed would be more profitable. The injury to its agricultural value was probable if not an inevitable result. It was expected to be offset, and was no doubt much more than offset, by the increase in its general value."

Again, there was no identifiable event, since the injury to the agricultural surface was gradual and, of course, self-induced.

On page 8 of his brief, respondent says that even if the flood adversely affected the ultimate value of the farmland, that injury is not deductible until a closed and completed transaction fixes the extent of the loss. He cites again *Hort v. Commissioner*, 313 U. S. 28, 33; *United States v. White Dental Company*, 274 U. S. 398, 401; *Citizens Bank of Weston v. Commissioner*, 252 F. 2d 425, 427 (C. A. 4th).

The petitioner in his petition for writ of certiorari cited decisions of this Court and others in tax cases to the effect that casualties constitute closed and completed transactions and identifiable events constituting grounds for loss. When such casualties occur, the extent of the loss is found without waiting for a sale or

abandonment, by determining the shrinkage in the value of the property, not in excess of its cost. *United States v. White Dental Manufacturing Company*, 274 U. S. 398; *Helvering v. Owens*, 305 U. S. 468; *Schearer v. Alderson* (C. A. 2d), 16 F. 2d 995; *Ferguson v. Commissioner* (C. A. 10), 59 F. 2d 893; *Rhodes v. Commissioner* (C. A. 6), 100 F. 2d 960; *Alcoma Association, Inc. v. U. S.* 385, 239 F. 2d 365.

Hence we are thrown back again to the question of whether this flood constituted a closed and completed transaction and an identifiable event.

The case of *Hort v. Commissioner, supra*, throws no light on the subject, since it did not involve a casualty and for other differences in the facts and issues as brought out in this brief. The case of *Citizens Bank of Weston v. Commissioner*, 252 F. 2d 425 (C. A. 4th), throws no light on the subject, since in that case there was no destruction to the land or building, hence, no casualty. The Court there on pages 426 and 427 said:

> "The building itself suffered no serious damage other than the slight damages which persist in the walls of the basement which causes the paint to scale. . . . The basement still houses the heating plant, but because the bank fears that flooding may occur and destroy its records, which are irreplaceable, it has not since 1950 used the basement for storage. . . . The Commissioner's position was and is that the flood has not materially altered the physical condition of the basement, and that there has been no loss of property; and further that although the bank's officers testified that it has permanently abandoned the basement

what is shown is merely a present nonuse, plus the retention of dominion so that it may upon future reconsideration again use this space as fully as before; and this is not enough to give rise to a recognized loss for tax purposes. . . .

Of course *United States v. White Dental Manufacturing Company*, 274 U. S. 389, shows that the loss of the use of the property by a casualty, even for a short period of time, can be a closed and completed transaction, and an identifiable event.

At the bottom of page 8 in his brief, the respondent says that the Court below properly described petitioner's authorities dealing with a "taking of property" as cases involving permanent impairment of usefulness. Petitioner again points out, as it did on page 14 of its petition, that neither the statute nor the regulations require that the injury be perpetual or even permanent. The only requisite is that there be a *loss*. Petitioner's loss was final, irreplaceable, irrepairable, though the water deprived it of use for one or two crop years only.

2. In Relying on the Hort Case, the Court Below Reached a Decision in Conflict With the Hort Case, and the Principle of Stare Decisis Established by This Court in Many Decisions.

On page 9 of his brief the respondent further discusses the case of *Hort v. Commissioner*, 313 U. S. 28, on which the Court below based its decision in the case at bar.

The taxpayer has shown on pages 14 to 19 of its petition that the *Hort* case is really not in point with the case at bar. The issue there was whether ". . . to

allow petitioner to reduce ordinary income actually received and reported by the amount of income he failed to receive." There was income in that case and not a casualty loss. It did not involve a casualty; the property involved had no cost or basis on which a loss could be taken; the transaction there was a voluntary one in which any burden which might have fallen upon the taxpayer was self-induced; there was a collection of a receivable and not the disposition of an asset in which a loss could be recognized. The Court in that case recognized that if there had been a disposition of a property interest, and if the property disposed of had a known cost, a loss might have been sustained and allowed.

Hence, the use of the *Hort* case as controlling the case at bar is in conflict with the decision in the *Hort* case.

It also conflicts with the principle established by this Court in *Higgins v. Commissioner*, 312 U. S. 212, 219; *American Steel Foundries v. Tri City Central Trades Council*, 257 U. S. 184, 211; *Supreme Lodge Knights of Pythias v. Smyth*, 245 U. S. 594, 597; and *Rutkin v. U. S.*, 343 U. S. 130, 138, wherein it is held that prior decisions are controlling only where the facts and issues are similar, and the same or substantially the same.

Contrary to respondent's attempt to make it appear so, petitioner is not endeavoring to take a deduction for loss of expected profits, but is only claiming a loss of capital invested in its farming lands, caused by the flood.

Conclusion.

In view of the facts: (1) that the petitioner had a casualty loss; (2) that decisions of this Court show, in conflict with the decision below, that a casualty loss can constitute a closed and completed transaction giving rise to a deductible loss; (3) that there is no requirement in the statute or regulations that the loss be perpetual or permanent; (4) that the lower Court violated the principle of *stare decisis* since it grounded its decision on the case of *Hort v. Commissioner, supra*, which did not involve a case where the taxpayer had a basis for the property involved, or a transaction in which a loss could be realized since there was no casualty or sale, but only a collection; — it is submitted that this Court should review the decision below and determine that taxpayer did have a deductible loss on account of the flood injury to its property.

Dated: September 19, 1962.

Respectfully submitted.

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Counsel for Petitioner.